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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1940.

No. 601.

PAUL W. SAMPSEL, as Trustee in Bankruptcy for the Estate of WILBUR J. DOWNEY, also known as W. J. DOWNEY,

*Petitioner,*

*vs.*

IMPERIAL PAPER AND COLOR CORPORATION,

*Respondent.*

## PETITIONER'S REPLY BRIEF.

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## PETITIONER'S REPLY BRIEF.

In view of respondent's vigorous contention that it bases its claim to priority upon an equitable lien on the funds derived by the trustee from the property recovered from the bankrupt's fraudulent transferee, Downey Wallpaper & Paint Co. (Respondent's Brief, pp. 11 and 12), we feel that a short reply is not out of place.

Respondent contends that equitable liens are recognized in California, and cites 16 Cal. Juris. on Liens, §10, p. 307, as authority. (See Respondent's Reply to Petition, p. 12.)

An examination of that section will disclose that all of the cases cited under Note 20, *Avery v. Clark,* 87 Cal. 619; *Dingley v. Bank of Ventura,* 57 Cal. 467, and *Ferger v. Allen,* 35 Cal. App. 738, are cases involving real property and in nowise involves personal property.

The case of *Carter v. Holt,* 28 Cal. App. 796 cited in Note 1, page 308, is a case wherein an attorney embezzled his client's funds invested $625.00 of them in an automobile which he was buying on a conditional sales contract, and when arrested for embezzelment he employed the defendant as his attorney and turned over the conditional sales contract on which $625.00 of his defrauded client's stolen money had been invested, to his attorney for services to be rendered in defending him. The defendant took the assignment of the contract with full knowledge that the $625.00 paid in on it constituted stolen money and the court declared a trust in favor of the defrauded client superior to that of the attorney who took the conditional sales contract with full knowledge of the fraud.

On the contrary, there is one decision of the Supreme Court of California which passes squarely on this question. *Moisant v. McPhee,* 92 Cal. 76. McPhee held a deed absolute to a certain tract of land in Mendocino county which deed, however, was given only for the purpose of securing an indebtedness owed to McPhee and his partner and which was held to be a real property mortgage. While this mortgage was in force and effect McPhee and his partner entered into an agreement with Warren, the mortgagor, whereby Warren was to peel bark on the property, dispose of the same, and apply the net proceeds after payment of expenses, on the balance of the indebtedness to McPhee. A quantity of bark was re-

moved in the summer of 1886 and the proceeds applied as agreed. In the summer of 1887 Warren peeled and prepared another quantity of bark on the mortgaged land. The defendant McPhee furnished him with supplies and money to meet his expenses, the advances amounting to about the sum of $1,000. After the bark was peeled, piled and sheltered by Warren, Warren sold it to the plaintiff Moisant for the sum of $1404.00, and executed a bill of sale to it. Plaintiff put a man in charge of the bark and posted notices on it that he was the owner. Warren not having paid his indebtedness for the advances made by McPhee in the sum of $1,000, took the peeled bark and shipped it to San Francisco and converted it to his own use. Plaintiff got judgment for conversion in the lower court. On appeal the Supreme Court of California said:

> "The only question, then is, did appellant acquire a valid lien upon the bark after it was severed from the trees? We are unable to see under what statute or rule of law it can be said that he did. A lien is created by contract, or by operation of law. (Civil Code, §2881.) Appellant was not a mortgagee or pledgee of the bark, and the evidence fails to show that any contract was made which would create a lien of any kind. *But if it be admitted that he had a lien, still, the possession of the bark was not taken by him, and hence his lien was void as against the plaintiff who purchased the property in good faith and for value.* (Civil Code, §3440.)" (Italics ours.)

Under the provisions of section 3440 of the Civil Code no distinction is made between purchasers and encumbrancers in good faith and creditors. The statute expressly provides that transfers or liens, where personal

property is concerned, with certain exceptions not material here, are conclusively presumed.

> "To be fraudulent, and therefore void, against those who are his creditors while he remains in possession, and the successors in interest of such creditors, and against any persons on whom his estate devolves in trust for the benefit of others than himself, and against purchasers or encumbrancers in good faith subsequent to the transfer."

Section 3430 of the Civil Code of California contains one definition of a creditor, as:

> "A creditor within the meaning of this title, is one in whose favor an obligation exists, by reason of which he is, or may become, entitled to the payment of money."

Section 3439.01 of the Civil Code of California defines creditor as:

> "A person having any claim, whether matured or unmatured, liquidated or unliquidated, absolute, fixed or contingent."

Section 3429 of the Civil Code of California defines a debtor as:

> "A debtor, within the meaning of this title, is one who, by reason of an existing obligation, is or may become liable to pay money to another, whether such liability is certain or contingent."

The trustee in bankruptcy as the successor in interest of the creditors of Wilbur J. Downey, was a creditor of the Downey Wallpaper & Paint Co., from the moment of the fraudulent transfer by that bankrupt of his property to his family corporation. The Downey Wallpaper &

Paint Co., from the moment of accepting the fraudulent transfer, which the Referee unhesitatingly found to have been made with the intent on Downey's part to cheat and defraud his creditors, certainly became one "who by reason of an existing obligation, is or may become liable to pay money to another." (Civil Code of California, Sec. 3429.) Therefore, it was manifestly impossible, in the face of the clear provisions of the statutory law of California (Section 3440), and the decision of the Supreme Court of the State of California in *Moisant v. McPhee,* 92 Cal. 76, which has never been overruled, for Imperial to have obtained an equitable lien on the assets of the Downey Wallpaper & Paint Co., unless those assets had been immediately delivered to it and continuously retained by it, as required under the provisions of section 3440 of the Civil Code.

*Bankruptcy Act,* Sec. 67-a;
*Bankruptcy Act,* Sec. 70-e, Subds. (1) and (2);
*Civil Code of California,* Sec. 3440;
*Moore v. Bay,* 284 U. S. 4.

It is well settled that the validity of liens is dependent upon the law of the state in which the lien has been attempted to be created.

*Straton v. New,* 283 U. S. 318, 17 Am. B. R. (N. S.) 630;
*Standard Oil Co. of New York v. Stevens,* 103 Vt. 1, 151 Atl. 507;
*Reese, Inc. v. United States,* 75 Fed. (2d) 9, 27 Am. B. R. (N. S.) 334 (C. C. A. 5th Cir.);

*Eggleston v. Birmingham Publishing Co.*, 15 Fed. (2d) 529, 8 Am. B. R. (N. S.) 714 (C. C. A. 5th Cir.);

*In Re McAllister*, 7 Fed. (2d) 9, 6 Am. B. R. (N. S.) 293 (C. C. A. 2nd Cir.);

*Remington on Bankruptcy*, 4th Ed., Sec. 1891.

If respondent's equitable lien theory fails, then certainly it is not entitled to any priority not granted to it under the provisions of section 64-b of the Bankruptcy Act.

*Southern Bell Telephone & Teelgraph Co. v. Caldwell*, 67 Fed. (2d) 802;

*United States Fidelity and Guaranty Co. v. Sweeney*, 80 Fed. (2d) 235;

*Buffum v. Barceloux*, 289 U. S. 227.

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Respectfully submitted,

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